MLP Earnings Offer Scant Support for Bears and Rich Kinder Gets Outplayed

We’re in earnings season and several Master Limited Partnerships provided updates this week that were generally unsurprising and reflected the stability of their business models. On Monday, Energy Transfer Partners (ETP) announced an 8% year-on-year increase in their distribution. Their GP Energy Transfer Equity (ETE) increased its distribution 37% on a year ago. These securities yield 9.5% and 5.5% respectively. ETE expects to close on its acquisition of Williams Companies (WMB) during 1Q16 which will add Williams Partners (WPZ) to the family of its MLPs it already controls (along with ETP they also control Sunoco LP and Sunoco Logistics Partners, LP).

Enterprise Products Partners (EPD) announced earnings showing 5% growth in distributions with 1.3X coverage. Its price rallied but still yields 5.8% based on its forecast next twelve months’ distribution. WPZ reported a 21% year-on-year increase in 2015 EBITDA driven by good performance from several fee-based projects. WPZ rallied on the news although curiously its future controlling entity ETE did not, even though ETE will ultimately benefit from this performance through its ownership of WMB. On the earnings call Williams noted that low prices for natural gas had led to about 900 million cubic feet (MMCF) per day of “shut-ins” whereby the E&P company temporarily stops producing natural gas because of the low market price or lack of infrastructure to get it to market. To put it in perspective, the U.S. consumes around 77 BCF per day, so this is a little over 1% of consumption. It didn’t seem to hurt results and they expect some of that production to come back online in the near term.

Overall, results were steady and unspectacular, which is usually the case. Distributions were as expected, growth guidance was generally reaffirmed. As I often say, the business performance is far less exciting on a quarterly basis than one might conclude by observing movements in MLP unit prices.

Kinder Morgan (KMI) also issued a $1.6BN mandatory convertible security, and regrettably it looks as if they were ripped off by their bankers. When they began contemplating alternatives to issuing equity, their stock was trading in the low $30s and their reluctance to sell equity at this level was understandable. Instead, they've sold equity at possibly as low as $27.56 (the lowest possible price at which conversion can occur). This is where their shares wound up when the deal was priced, no doubt depressed by the underwriters shorting the stock to hedge the new convertible issue. The 9.75% coupon they're paying on this security is higher than either KMI's debt or equity even though it sits between those obligations in seniority on their balance sheet, and the only risk being taken by the investor is the possibility of being converted into common at $27.56 at a time when the market price is below that. While the rating agencies treat the issue as equity, those bearish on the security will argue it's high-cost leverage and that management is signaling they're worried that the stock is headed much lower than $27.56. The bulls will see it as super expensive, dilutive equity. It's inconceivable that KMI expected this outcome; they would have been far better off continuing with their original plan of regular equity issuance. A rare lose-lose from Rich Kinder.

My new book, *Wall Street Potholes*, was just released and it's aimed at retail investors. I may have to start working on another version written for capital markets clients outfoxed by their bankers.

Overall, there wasn't much over the past week in fundamental news to provide much support to bears. The most negative issue might be the continued volatility and relatively high dividend yields.

We are invested in EPD, ETE, KMI and WMB